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COP27 Update: The U.S. Weighs in With Regulatory Proposals

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As COP27, in Sharm El Sheikh, Egypt, enters its second and final week, the rate of climate-reduction initiatives by regulators and global leaders continues unabated. In the U.S., on November 10, the Biden Administration announced new federal rules that will require federal government suppliers to disclose emissions in an effort to protect supply chains from climate-related risks. The White House **press release** accompanying the announcement states that the U.S. federal government is the world's largest buyer of goods and services—purchasing over $630 billion in the last fiscal year—and that over half of federal contractors were already disclosing "climate related information" through CDP. For further details on CDP, please see our recent Cadwalader Climate **post** discussing developments on the platform.

The proposed Federal Supplier Climate Risks and Resilience Rule will require "the largest suppliers including Federal contractors receiving more than $50 million in annual contracts" to publicly disclose "Scope 1, Scope 2, and relevant categories of Scope 3 emissions, disclose climate-related financial risks, and set science-based emissions reduction targets." Federal contractors with more than $7.5 million but less than $50 million in annual contracts would be required to publicly report Scope 1 and Scope 2 emissions. Federal contractors with less than $7.5 million in annual contracts would be exempt from the rule.

And one day later, on November 11, the EPA released an **update** to its 2021 proposed methane reduction rule. The supplemental rule includes, among other things, a "Super Emitter Response Program" that would require oil and gas operators to identify and respond to large leaks and emissions events identified by EPA-approved third parties. In addition, the proposed rule would further limit the use of flares to burn off unwanted methane from oil and gas wells. According to the Agency, the proposed rule as supplemented would reduce methane emissions from the U.S. oil and gas sector by 87 percent below 2005 levels by 2030.

Disclosure: TNFD Publishes Updated Draft Framework

November 15, 2022

Disclosure

By Simon Walsh
Special Counsel | Global Litigation

On November 4, the Taskforce on Nature-Related Financial Disclosures (TNFD) published the **third iteration** of its beta framework for nature-related risk management and disclosures. The draft framework, which is an update to the second draft released in June, is designed to help companies report on their nature-related risks and impacts. It also includes disclosure requirements and guidance on how to establish science-based targets. According to the framework's executive summary, TNFD is now half-way through its planned two-year "design and development phase" in building the framework. The fourth draft is scheduled for release in March 2023, prior to final recommendations being published in September 2023. The taskforce consists of 40 members, including financial institutions, corporations, and markets service providers, and is assisted by a forum of over 750 members together with 18 scientific organizations and standard setting bodies.

The executive summary of the framework states that the taskforce's aims are to:

- "Help drive alignment with the emerging global reporting baseline under development by the International Sustainability Standards Board and with best practice standards and tools already used by market participants today;"
- Provide a readily-adaptable and flexible "approach to materiality to accommodate the preferences and regulatory requirements of report preparers and report users from organizations of different sizes and across different jurisdictions;"
- "Encourage early action by companies and financial institutions to begin reporting nature-related dependencies, impacts, risks and opportunities;" and
- Offer a structured path to increase disclosure over time, given the Task Force's view that nature-related issues are "a rapidly growing strategic imperative for sound governance, strategy, risk management and capital allocation."

Taking the Temperature: This TNFD initiative is notable as an effort to design a voluntary framework using an extensive, iterative development process involving a large number of stakeholders spanning different sectors. The TNFD adopted this approach because there currently is no standard framework for these types of disclosures coupled with the well-recognized need for and benefits accruing from a globally consistent approach. In general, the issue of governance and disclosures concerning biodiversity and nature have been taking on increasing prominence in the overall sustainability discussion. We recently reported that a group of over 300 companies, in advance of the nature-focused December COP15 in Montreal, signed a statement asking governments to mandate that

“large and transnational businesses and financial institutions assess and disclose their impacts and dependencies on biodiversity, by 2030,” in light of the fact that companies generally provide far less nature-related disclosures (i.e., regarding deforestation or water security) than other climate-related disclosures. And, as we also discussed the Deputy Governor of the Banque de France, the French central bank, Sylvie Goulard, stated in a speech on October 24 that central banks need to take more aggressive action regarding nature-related risk, in part because of their complexity and also because “shocks” in one sector can have significant impacts on other sectors. We anticipate that this trend will continue: Regardless of whether an issuer or financial institution is in a single or double materiality jurisdiction—whereby information is material not only because of its potential impact on the issuer but also because of the issuer’s impact on climate—attempting to make and justify distinctions between an issuer’s impact on the environment and whether that impact could in turn “boomerang” to have a material impact on the issuer will become exceedingly difficult. As a result, companies and their directors should increase their assessments of governance and disclosures concerning nature-related impacts, regardless of whether they are mandated by government regulation.

Regulation: IOSCO Begins Consultation on Carbon Markets

November 15, 2022

Regulation

By Peter Malyshev
Partner | Financial Services

The International Organization of Securities Commissions (IOSCO), an international policy forum for securities regulators, has **announced** the publication of a consultation report and discussion paper. The 90-day public consultation covers "recommendations for establishing sound Compliance Carbon Markets" and "key considerations for enhancing the resilience and integrity of Voluntary Carbon Markets. . . ." **The Compliance Carbon Markets (CCMs) Consultation Report** and the **Voluntary Carbon Markets (VCMs) Discussion Paper** are open to public comment until February 10, 2023. IOSCO is asking for market participants to give feedback on "how to foster fair and functional markets and increase structural resilience to ensure these markets achieve their stated purpose, i.e., the environmental objectives upon which their existence is based." The report on CCMs (which are created and regulated by mandatory governmental carbon-reduction regimes) offers various recommendations for jurisdictions that are looking to establish compliant carbon markets as a way to achieve their obligations under Article 6 of the Paris Agreement. The report on VCMs (which operate outside of compliance markets) details characteristics that can "foster sound carbon credit markets," together with weaknesses that currently limit the growth of the carbon credit markets. The report requests that respondents consider the role that financial regulators should play in overseeing these markets.

Announcing the publication of the reports at COP27, Jean Paul Servais, IOSCO Chairman, IFRS Foundation Monitoring Board Chair and Chairman of the Belgium Financial Services and Markets Authority, said, "In recent years, carbon markets have gained significant importance as a mechanism for corporates, and society in general, to facilitate their transition towards net zero. However, they have so far fallen short of their objectives. No market can function without appropriate levels of integrity and, transparency, and liquidity so IOSCO today hopes to lend its international, market expertise to help develop appropriate frameworks for sound and well-functioning carbon markets, focusing on promoting integrity and liquidity and increasing transparency to facilitate price discovery."

Taking the Temperature: IOSCO is a significant force in the regulatory landscape with its membership regulating over 95% of the world's securities markets in 130 jurisdictions. Its proposals will likely carry great weight with their member regulators. The carbon offset market has come under significant scrutiny recently due to concerns that product inconsistencies and lack of scrutiny may be leading to greenwashing. There are also concerns that carbon offset markets can disincentivize or distract corporate actors from the primary objective of reducing emissions. The IOSCO consultation was launched in large part in response to these concerns. Of course, the effectiveness of regulatory

activity in promoting well-functioning and high-volume carbon markets remains to be seen, and the future verdict on that issue will have to await the further evolution of any such regulation.

Notably, the U.S. Commodity Futures Trade Commission's (CFTC) Chair, Rostin Behnam, was recently appointed as the vice chair of IOSCO. Rostin is an avid advocate for the development of carbon markets in the U.S., and the CFTC has been active in finding market solutions to climate change. The CFTC has also published several reports on VCMs and in June 2022 hosted a VCM convening. The CFTC is currently working on a report regarding the impact of climate change on the U.S. financial market.

Disclosure: UN Report on Net-Zero and Greenwashing

November 15, 2022

Disclosure

By Jason Halper
Partner and Co-Chair | Global Litigation

The United Nations' High-Level Expert Group on the Net Zero Emissions Commitments of Non-State Entities has published a **report** titled, *Integrity Matters: Net Zero Commitments by Businesses, Financial Institutions, Cities and Regions*. The report establishes five principles to guide setting and achieving net-zero targets, together with ten recommendations for what non-state actors should consider at each stage of the process to becoming net-zero aligned.

The report includes a series of recommendations relating to avoiding greenwashing, including that private sector companies:

- should not claim to be net-zero compliant while continuing to build or invest in new fossil fuel supply;
- should not purchase inexpensive carbon credits that "often lack integrity" instead of cutting emissions across their own value chain;
- should focus on reducing emissions across their full value chain (i.e., Scopes 1, 2 and 3);
- should not lobby to undermine government climate policies – either directly or via trade associations or other bodies; and
- should, in order to "tackle greenwashing and ensure a level playing field," move from voluntary initiatives to regulated net-zero requirements.

In her note to the report, Catherine McKenna, the Chair of the Expert Group and Canada's former Minister of Environment and Climate Change, stated that: "We are making progress but we are still too far from where we need to be. … To prevent dishonest climate accounting and other actions designed to circumvent the need for deep decarbonization, we emphasize that non-state actors must report publicly on their progress with verified information that can be compared with peers."

Taking the Temperature: The UN Report underscores the ever-increasing focus on greenwashing by regulators, corporate stakeholders, and NGOs, particularly in the absence of global consensus on what constitutes greenwashing. However, the recommendations in the Report, while not revolutionary, could be construed to significantly expand the concept of greenwashing. Typically, greenwashing refers to falsely enhancing a product's or business' sustainability profile. The UN Report expands that concept to various areas of corporate activity, such as using inexpensive carbon credits, investing in fossil fuel production, or taking affirmative steps to undermine government climate initiatives, which expressly includes inconsistent

lobbying activity. By going that far, the UN Report is effectively incorporating policy issues still subject to fierce debate, including the definition of false sustainability claims. For instance, while ceasing new fossil-fuel supply may be beneficial from a greenhouse gas emissions perspective, fossil fuels are necessary to meet current and foreseeable energy demand and to build the green energy infrastructure necessary to ultimately reduce global fossil fuel energy consumption. By painting with such a broad brush under a greenwashing label, the UN Report obscures the complexities involved and potentially sows further confusion about what constitutes a sustainable business or product.